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No. 98-1101

In the Supreme Court of the United States

OCTOBER TERM, 1998

ROHN F. DRYE, JR., ET AL., PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTION PRESENTED

Whether the interest of an heir in an estate constitutes "property" or a "right[] to property" to which the federal tax lien attaches under 26 U.S.C. 6321 even though the heir thereafter purports retroactively to disclaim the interest under state law.

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statement	1
Argument	5
Conclusion	14

TABLE OF AUTHORITIES

Cases:

Bank One Ohio Trust Co. v. *United States*, 80 F.3d 173 (6th Cir. 1996)	6, 7
Clark v. *Gauntt*, 161 S.W.2d 270 (Tex. 1942)	11
Kimura, In re, 969 F.2d 806 (9th Cir. 1992)	7
Leggett v. *United States*, 78 A.F.T.R.2d (RIA) 96-6344 (S.D. Tex. 1996), rev'd, 120 F.3d 592 (5th Cir. 1997)	4, 9, 10, 11, 13
Little v. *United States*, 704 F.2d 1100 (9th Cir. 1983)	7
Mapes v. *United States*, 15 F.3d 138 (9th Cir. 1994)	4, 9, 11, 12
Raihl, In re, 152 B.R. 615 (B.A.P. 9th Cir. 1993)	7
Terwilligers Catering Plus, Inc., In re, 911 F.2d 1168 (6th Cir. 1990), cert. denied, 501 U.S. 1212 (1991)	7
21 West Lancaster Corp. v. *Main Line Restaurant, Inc.*, 790 F.2d 354 (3d Cir. 1986)	7
United States v. *Bess*, 357 U.S. 51 (1958)	6, 8
United States v. *Comparato*, 850 F. Supp. 153 (E.D.N.Y. 1993), aff'd, 22 F.3d 455 (2d Cir.), cert. denied, 513 U.S. 986 (1994)	8, 13
United States v. *Irvine*, 511 U.S. 224 (1994)	9, 12
United States v. *Mitchell*, 403 U.S. 190 (1971)	9
United States v. *National Bank of Commerce*, 472 U.S. 713 (1985)	4, 6, 8, 11

Cases—Continued: Page

United States v. *Rodgers*, 461 U.S. 677 (1983) 6, 8
United States v. *Stonehill*, 83 F.3d 1156 (9th Cir.), cert. denied, 519 U.S. 992 (1996) 6-7

Statutes:

Internal Revenue Code (26 U.S.C.):
§§ 2001-2704 9
§ 2518 9
§ 6321 ..... 2, 4, 5, 6, 7, 9, 10, 11, 13
§ 6322 6
§ 6502 6
§ 7426 3
Ark. Code Ann. (Michie 1987):
§ 28-2-101 2
§ 28-2-108 2
§ 28-9-203 2

Miscellaneous:

William D. Elliot, *Federal Tax Collection, Liens, and Levies* (2d ed. 1998 Cum. Supp. No. 1) 13
Steve R. Johnson, *Fog, Fairness, and the Federal Fisc: Tenancy-By-The Entireties Interests and the Federal Tax Lien*, 60 Mo. L. Rev. 839 (1995) 6

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-18a) is reported at 152 F.3d 892. The orders of the district court (Pet. App. 19a-24a, 25a-27a) are unreported.

JURISDICTION

The judgment of the court of appeals was entered on August 17, 1998. The petition for a writ of certiorari was filed on November 16, 1998 (a Monday). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Prior to June 1991, the Internal Revenue Service assessed income taxes and various penalties against

petitioner Rohn Drye.[1] Because petitioner failed to pay these assessments, the Service filed notices of tax lien upon "all property and rights to property" belonging to him (26 U.S.C. 6321). Pet. App. 3a, 21a.

In August 1994, petitioner's mother died intestate, leaving an estate with a total value of approximately $233,000 to petitioner as her sole legal heir. At the time of his mother's death, petitioner was insolvent and owed the government approximately $325,000 on the unpaid tax assessments for which notices of outstanding liens had been filed. Pet. App. 3a, 22a.

Petitioner was appointed administrator of his mother's estate on August 17, 1994. In February 1995, petitioner executed and filed in the probate court an instrument entitled "Disclaimer and Consent" in which he disclaimed his entire interest in his mother's estate. Pet. App. 3a, 21a. Pursuant to that disclaimer, the estate passed by operation of state law to petitioner's daughter, Theresa Drye. *Id.* at 21a.[2] Petitioner's daughter concurrently established a trust (The Drye

[1] Unless otherwise noted, all references to "petitioner" are to Rohn Drye.

[2] Under Arkansas law, upon the death of the decedent intestate, real property passes immediately to the decedent's heirs and personal property passes to the personal representative for distribution to the heirs. Ark. Code Ann. § 28-9-203 (Michie 1987); see Pet. App. 32a-33a. An heir may disclaim his interest in the estate. Ark. Code Ann. § 28-2-101 (Michie 1987); see Pet. App. 30a-31a. If such a disclaimer is filed, state law creates a legal fiction that the disclaimant predeceased the decedent, with the result that the disclaimant's share of the estate passes to the next person in line to receive that share. Ark. Code Ann. § 28-2-108 (Michie 1987); see Pet. App. 32a. By filing such a disclaimer, an heir may prevent his state-law creditors from obtaining payment from that share of the estate. Ark. Code Ann. § 28-2-108 (Michie 1987); see Pet. App. 32a.

Family 1995 Trust), the beneficiaries of which were petitioner, his wife, and his daughter. *Id.* at 3a-4a, 22a. Petitioner resigned as administrator of the estate and his daughter replaced him. *Id.* at 3a, 22a. The state probate court thereupon authorized the distribution of the estate property to petitioner's daughter, who used the property to fund the trust. *Id.* at 3a-4a.

After petitioner revealed his beneficial interest in this family trust during negotiations with the Internal Revenue Service in 1995, the government filed a notice of tax lien against the trust, as Drye's nominee. That lien encumbers the real and personal property of the trust. Pet. App. 4a, 21a. The Service also levied upon accounts held in the trust's name at an investment company. The account proceeds of $134,004.33 were paid to the government pursuant to the levy. *Id.* at 4a, 23a.

2. On May 1, 1996, the trust filed a wrongful levy suit against the United States in federal district court under Section 7426 (26 U.S.C. 7426). The trust contended that, because of the disclaimer of petitioner's interest in the estate, petitioner never held an interest in that estate to which the federal tax liens could attach. Pet. App. 2a, 26a.

The district court granted the government's motion for summary judgment. Pet. App. 19a-24a. The court concluded that petitioner "obtained a vested interest in the estate property of his mother upon her death to which the federal tax liens properly attached so that the state disclaimer law that was later invoked was incapable of removing those federal liens." *Id.* at 23a. In response to the trust's motion for reconsideration, the court emphasized that federal law determines the proper application of federal tax liens and that "a state disclaimer law that is later invoked after the liens

properly attached cannot remove those federal liens." *Id.* at 26a.

3. The court of appeals affirmed. Pet. App. 1a-18a. The court explained that, under the federal tax lien statute, the court is to look to state law to determine "whether a given set of circumstances creates a right or interest" (*id.* at 12a) and then look to federal law to determine whether that right or interest constitutes "property" or "rights to property" (26 U.S.C. 6321) to which the federal tax lien attaches (Pet. App. 12a-13a (citing *United States* v. *National Bank of Commerce*, 472 U.S. 713, 727 (1985))). See also *id.* at 6a-8a.[3] The court held that an interest in property under state law constitutes "property" or "rights to property" under federal law (to which the federal tax lien attaches under 26 U.S.C. 6321) if the interest is transferable and has pecuniary value (Pet. App. 7a, 14a).

The court of appeals concluded that petitioner's right to inherit the property of his mother's estate satisfied this standard because that right was transferable and had pecuniary value (Pet. App. 8a, 14a). Petitioner's interest thus represented "property" or "rights to property" for purposes of the federal tax lien statute, and the tax liens filed against petitioner attached to his right to inherit his mother's estate. *Id.* at 13a.

The court explained that petitioner's subsequent disclaimer of his interest under state law could not extinguish the federal liens that previously attached to

[3] The court stated (Pet. App. 12a) that it parted company with the Fifth Circuit's decision in *Leggett* v. *United States*, 120 F.3d 592 (1997), and the Ninth Circuit's decision in *Mapes* v. *United States*, 15 F.3d 138 (1994), because those cases erroneously apply state law, rather than federal law, in ascertaining whether the interest possessed by the taxpayer constitutes "property" or "rights to property" under Section 6321.

that interest. The fact that, for purposes of state law, the disclaimer is treated as if it relates back to the date of the decedent's death does not mean that, at the time the lien attached, petitioner held no "property" or "rights to property" in the estate. Because the federal liens validly attached to that property *before* the disclaimer was made, petitioner's subsequent efforts to dispose of his interest could not defeat the federal lien. Title to the property transferred to the trust remained subject to the preexisting federal tax lien, and the levy on the assets of the trust to satisfy petitioner's debt was therefore not wrongful. Pet. App. 4a-5a, 17a-18a.

ARGUMENT

The court of appeals correctly applied principles that have long been established in the decisions of this Court. Although two earlier court of appeals decisions reach results that cannot be reconciled with the result in this case (see note 3, *supra*), those earlier cases arose in sufficiently distinct contexts that it cannot be said that they squarely conflict with the present decision. If a sufficiently clear conflict hereafter develops, we would acknowledge that review by this Court would be appropriate. At the present time, however, it appears that a uniform resolution of this recurring issue may hereafter be obtained in the courts of appeals. Review by this Court of the question presented in this case is thus unnecessary at this time.

1. The court of appeals correctly applied this Court's longstanding precedent under Section 6321 of the Internal Revenue Code. That Section provides that, "[i]f any person liable to pay any tax neglects or refuses to pay the same after demand, the amount * * * shall be a lien in favor of the United States upon *all property and rights to property*, whether real or personal, be-

longing to such person." 26 U.S.C. 6321 (emphasis added).[4] As this Court has frequently emphasized, although "state law controls in determining the nature of the legal interest which the taxpayer had in the property," whether that interest is sufficient to constitute "property" or "rights to property" under Section 6321 is determined solely as a matter of federal law and "state law is inoperative" for this purpose. *United States* v. *National Bank of Commerce*, 472 U.S. 713, 722 (1985) (quoting *United States* v. *Bess*, 357 U.S. 51, 56-57 (1958)). See also *United States* v. *Rodgers*, 461 U.S. 677, 683 (1983); *Bank One Ohio Trust* Co. v. *United States*, 80 F.3d 173, 175-176 (6th Cir. 1996).[5]

There is no statutory definition of the terms "property" and "rights to property" as used in Section 6321. Courts have routinely concluded, however, that an interest in property constitutes "property" or a "right[] to property" under the statute if it has pecuniary value and is transferable. See *United States* v. *Stonehill*, 83 F.3d 1156, 1159-1160 (9th Cir.) (chose-in-action is subject to federal tax lien because it has pecuniary value and is transferable), cert. denied, 519 U.S. 992 (1996); *In re Kimura*, 969 F.2d 806, 810-811 (9th Cir. 1992) (liquor license is subject to federal tax lien because it has pecuniary value and is transferable); *In re Terwilliger's Catering Plus, Inc.*, 911 F.2d 1168, 1171-1172 (6th Cir. 1990) (same), cert. denied, 501 U.S. 1212 (1991); *21 West Lancaster Corp.* v. *Main Line Restaurant, Inc.*, 790 F.2d 354, 357-358 (3d Cir. 1986) (same); *Little* v. *United States*, 704 F.2d 1100, 1104-1106 (9th Cir. 1983) (right of redemption, although classified as a "privilege" under state law, is subject to federal tax lien because it has pecuniary value and is transferable).[6]

Applying that established principle to the facts of this case, the court of appeals correctly held (Pet. App. 7a-8a) that the interest that petitioner acquired in his mother's estate at the time of her death constituted "property" or a "right to property" because it had pecuniary value and was transferable. See also note 5, *supra*. At the time of his mother's death, petitioner acquired the right to receive the entire value of the estate (approximately $233,000) less its administrative expenses. *Id.* at 3a. That right plainly had a substantial pecuniary value. Moreover, as the court of appeals noted (*id.* at 8a), that right was transferable under Arkansas law. Because the interest thus obtained by

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[4] The lien arises as of the date of assessment and continues until the underlying tax liability is satisfied or the statute of limitations on collection bars action. 26 U.S.C. 6322, 6502.

[5] See also Steve R. Johnson, *Fog, Fairness, and the Federal Fisc: Tenancy-By-The-Entireties Interests and the Federal Tax Lien*, 60 Mo. L. Rev. 839, 858 (1995) (footnote omitted):

> The predominance of substance over state-created labels and formalities is demonstrated by the fact that the federal tax lien attaches to economic rights and interests even if the applicable state law does not classify them as property interests. For example, in *United States* v. *National Bank of Commerce*, the right to withdraw money from a bank account was not called a property right by Arkansas law but nonetheless was held to be a sufficient property interest for federal tax collection purposes.

[6] The taxpayer's interest may not need to be transferable to constitute a "right[] to property" for purposes of Section 6321. In *Bank One Ohio Trust Co.* v. *United States*, 80 F.3d at 175-177, the Sixth Circuit held that a beneficiary's interest in a spendthrift trust, which was not transferable for state-law purposes, was subject to the federal tax lien. See also *In re Raihl*, 152 B.R. 615, 618 (B.A.P. 9th Cir. 1993) ("The inalienability of the pension interests does not destroy their character as property or immunize the interest from the attachment of a federal tax lien.").

petitioner was both valuable and transferable, it constitutes "property" or "rights to property" to which the federal tax lien could—and in fact did—attach.

By subsequently disclaiming his right to his intestate share of the estate, petitioner transferred that right to his daughter, who thereafter transferred the underlying property to the trust. Those transfers, however, do not undermine the effectiveness of the tax lien—any property subject to a federal lien passes "cum onere." *United States* v. *Bess*, 357 U.S. at 57. As the court of appeals correctly held in this case, petitioner's subsequent disclaimer of his interest in the estate did not defeat the previously-attached federal tax lien because, "once a lien has attached to an interest in property, the lien cannot be extinguished * * * simply by a transfer or conveyance of the interest." *United States* v. *Rodgers*, 461 U.S. at 691 n.16.

This conclusion also flows from the established principle that, "[o]nce it has been determined that state law creates sufficient interests in the taxpayer to satisfy the requirements of the statute, state law is inoperative, and the tax consequences thenceforth are dictated by federal law." *United States* v. *National Bank of Commerce*, 472 U.S. at 722 (quoting *United States* v. *Bess*, 357 U.S. at 57) (internal brackets and quotation marks omitted). In particular, "legal fictions" adopted by state law under which a subsequent disclaimer of a property interest is treated as if it were effective retroactively do not retroactively destroy an existing federal lien. See, *e.g.*, *United States* v. *Comparato*, 850 F. Supp. 153, 159 (E.D.N.Y. 1993) ("state law is relevant only to the determination of whether a taxpayer has a right to certain property, not to whether he can thereafter renounce his right"), aff'd, 22 F.3d 455 (2d Cir.), cert. denied, 513 U.S. 986 (1994). For

example, in *United States* v. *Irvine*, 511 U.S. 224, 240 (1994), this Court held that a disclaimer of a remainder interest in a testamentary trust is a taxable gift by the disclaimant, even though under state law the disclaimer is treated as relating back to the original creation of the trust. The Court explained that "Congress had not meant to incorporate state-law fictions as touchstones of taxability" and that federal taxation looks to the reality of the transaction and is not "struck blind by a disclaimer." *Ibid.* See also *United States* v. *Mitchell*, 403 U.S. 190 (1971) (although a wife's renunciation of a marital interest was deemed retroactive in effect under state law, that state-law fiction is not operative in determining the wife's liability for tax on her share of the community income realized before the renunciation); *United States* v. *Comparato*, 22 F.3d 455, 457 (2d Cir. 1994) ("once the federal liens attached * * * , [the taxpayers'] subsequent renunciations pursuant to state law were not effective against the federal liens").[7]

2. Even though the decision in this case merely applies principles long set forth in this Court's decisions under Section 6321, two prior court of appeals decisions have reached results that are inconsistent with the decision in this case. In *Leggett* v. *United States*, 120 F.3d 592 (5th Cir. 1997), and *Mapes* v. *United States*, 15 F.3d 138 (9th Cir. 1994), the courts held that a renunciation of an inheritance is effective to invalidate a federal tax lien. Although those earlier decisions are inconsistent with the decision in this case, they arise in

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[7] Certain types of "qualified" disclaimers are given effect for purposes of the federal wealth-transfer taxes (Subtitle B, §§ 2001-2704 of the Internal Revenue Code) under Section 2518 of the Internal Revenue Code. See 26 U.S.C. 2518. Petitioner has not contended that his disclaimer qualifies under this provision.

sufficiently distinct contexts that it cannot be said that they squarely conflict with the present decision.

a. In *Leggett*, the government mistakenly represented to the court of appeals that the case involved solely a question of *state* law. The government failed to point out that the question whether a particular interest constitutes "property" or "rights to property" within the meaning of Section 6321 is a question of federal law. The Fifth Circuit was thereby led erroneously to give retroactive effect to the taxpayer's state-law renunciation of his property interest.

In *Leggett*, as in the present case, the United States acquired a tax lien in all property and rights to property of the taxpayer before she obtained an interest in her aunt's estate. And, as in the present case, the taxpayer disclaimed her interest in the estate and claimed, as a result, that the tax lien became invalid. The district court held in favor of the government. *Leggett* v. *United States*, 78 A.F.T.R.2d (RIA) 96-6344 (S.D. Tex. 1996), rev'd, 120 F.3d 592 (5th Cir. 1997). The court stated (i) that "whether a taxpayer has an interest in property to which a tax lien may attach" is controlled by "[s]tate law" and (ii) that the taxpayer had such an interest in that case because, under Texas law, title to property vests in the beneficiaries immediately upon a decedent's death. *Id.* at 96-6346. The court concluded that the federal lien, once attached, could not be divested by a subsequent state-law disclaimer. *Id.* at 96-6347.

In reversing that decision, the Fifth Circuit followed the erroneous submission of the government in stating that the question whether the taxpayer had a property interest to which the federal tax lien could attach is solely a question of state law. 120 F.3d at 594. See also *id.* at 597 ("Section 6321 adopts the state's definition of

property interest."). The court concluded that the right to renounce an interest in an estate did not constitute "property" under Texas law. Because a "property" interest did not exist under state law, the court held that the taxpayer "never had a property right" to which the federal tax lien could attach under Section 6321. 120 F.3d at 596.

In *Leggett*, the government failed to advise the Fifth Circuit that the controlling decisions of this Court clearly establish that whether an interest created under state law constitutes "property" or "rights to property" for purposes of Section 6321 is a question of *federal* law. *United States* v. *National Bank of Commerce*, 472 U.S. at 727. Since the taxpayer's right to receive the assets of the estate was plainly a valuable right and was transferable (*Clark* v. *Gauntt*, 161 S.W.2d 270, 272 (Tex. 1942)), it constituted a "right[] to property" to which the tax lien would attach under federal law. Because the court in *Leggett* was misinformed by the government as to the applicable law, and because that court has not had an opportunity to revisit this issue, it cannot be said that the decision in *Leggett* represents a fully mature conflict with the present case.

b. In *Mapes*, the taxpayer's mother died, leaving him one-half of her estate. At the time of his mother's death, the taxpayer and his wife owed the United States approximately $500,000 in outstanding taxes. One week after his mother's death, in an effort to prevent the government's lien from attaching to his interest in his mother's estate, the taxpayer renounced his interest in favor of his children. 15 F.3d at 139.

The government argued in *Mapes* that (i) upon his mother's death, the taxpayer acquired a vested interest in his mother's estate under the applicable local law, (ii) an existing federal tax lien attached at that time to that

vested interest and (iii) the taxpayer's subsequent renunciation of his interest did not defeat the existing federal lien. 15 F.3d at 139-140, 141-142 n.4. The Ninth Circuit rejected the government's contention. While acknowledging that "federal law is controlling on the question of whether Mapes had a lienable interest in his mother's estate," the court concluded that "the fundamental question [is] whether Mapes had any interest in the property, lienable or not." *Id.* at 140. The court held that "[f]or the answer to that question we must look to state law, not federal law." *Ibid.* Noting that the taxpayer's renunciation (one week after his mother's death) was timely and valid under state law, the court held that, because the renunciation related back to the date of death under state law, the taxpayer never had any interest in the property to which the federal tax lien could attach. *Ibid.* The court concluded that the federal tax lien was therefore ineffective against the taxpayer's interest in his mother's estate. *Id.* at 140-141.

The conclusion of the court of appeals in *Mapes*—essentially that a renunciation under state law can relate back to extinguish retroactively a taxpayer's property interest to which a federal tax lien would otherwise have remained attached (thus defeating the lien)—cannot be reconciled with the reasoning of this Court in *United States* v. *Irvine*, *supra*. In *Irvine*, which was decided three months *after* the Ninth Circuit entered its decision in *Mapes*, the Court emphasized that, in determining whether a taxpayer possesses an interest in "property" for estate and gift tax purposes, federal courts are to look to factual realities and not be "struck blind" by state-law "legal fiction[s]" that permit renunciations of ownership to be retroactively effective. 511 U.S. at 240. That holding in *Irvine* provides direct

support for the decision of the court of appeals in this case and for the similar decision of the Second Circuit in *United States* v. *Comparato*, 22 F.3d at 457:

> The Supreme Court decision in *United States v. Irvine* supports the result reached in *Comparato*. In *Irvine* * * * [t]he Supreme Court reaffirmed the principle followed in *Comparato* that "although state law creates legal interests and rights in property, federal law determines whether and to what extent those interests will be taxed." The Court then applied federal law in determining the validity of Irvine's disclaimer for federal gift tax purposes.

William D. Elliot, *Federal Tax Collections, Liens, and Levies* ¶ 9.09[3][d][ii], at S9-10 (2d ed. 1998 Cum. Supp. No. 1) (footnotes omitted).

In any future case presenting the same issue, the Ninth Circuit would be required to consider the effect of this Court's decision in *Irvine* upon the reasoning and holding of *Mapes*.[8] Until the Ninth Circuit has had an opportunity to reconsider this issue, and to give effect to this Court's decision in *Irvine*, there is no direct and mature conflict among the circuits that requires resolution by this Court.

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[8] To be sure, the Fifth Circuit in *Leggett* purported to distinguish *Irvine* on the grounds that *Irvine* involved the gift tax provisions, which do not adopt state law, whereas the statute at issue in *Leggett* (and here), Section 6321, "adopts the state's definition of property interest." *Leggett*, 120 F.3d at 597. But since, as we have shown, Section 6321 does *not* adopt the state's definition of "property" or "rights to property," the Fifth Circuit's attempt to distinguish *Irvine* is unavailing. See pp. 10-11, *supra*.

CONCLUSION

The petition for writ of certiorari should be denied.

Respectfully submitted.

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